

Message Text

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ACTION EUR-12

INFO OCT-01 EA-12 ISO-00 AID-05 CIAE-00 COME-00 EB-08
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R 051759Z JAN 78
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TO SECSTATE WASHDC 1753
TREASURY DEPT WASHDC
INFO AMEMBASSY BONN
AMEMBASSY PARIS
AMEMBASSY ROME
AMEMBASSY TOKYO

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USOECD ALSO FOR EMBASSY

E.O. 11652: N/A
TAGS: EFIN, UK
SUBJECT: EDITORIAL REACTION TO ANNOUNCEMENT OF MORE
ACTIVE U.S. FOREIGN EXCHANGE INTERVENTION

THE ANNOUNCEMENT OF INCREASED U.S. INTERVENTION IN FOREIGN EXCHANGE MARKETS HAS YET TO ENGENDER EXTENSIVE EDITORIAL COMMENT. THE OPINIONS THAT HAVE BEEN EXPRESSED REFLECT, IN THE MAIN, THE DOMESTIC IMPACT OF FOREIGN EXCHANGE MOVEMENTS.

1. THE LEX COLUMN OF THE FINANCIAL TIMES WRITES:
QUOTE: ONE SAFE PREDICTION FOR 1978 WAS THAT THE U.K.'S DOMESTIC FINANCIAL MARKETS WOULD HAVE TO CONTEND WITH THE DESTABILISING INFLUENCE OF THE DOLLAR, AND THIS MESSAGE IS COMING THROUGH WITH A VENGEANCE IN THE FIRST WEEK OF THE NEW YEAR. YESTERDAY MORNING STERLING CAME WITHIN A
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WHISKER OF \$2 IN LONDON AT ONE STAGE, BUT THEN PROFIT TAKING SET IN, AND BY LATE LAST NIGHT, FOLLOWING THE UNVEILING OF THE U.S. ADMINISTRATION'S AGGRESSIVE NEW INTERVENTION POLICY, RATES IN NEW YORK FELL QUICKLY TO CLOSE AT \$1.8750. THIS DRAMATIC TURNAROUND COMES AT A MOMENT WHEN THE GILT-EDGED MARKET IS BEING BUOYED UP BY THE STRENGTH OF STERLING AND BY THE PROSPECTS OF LOWER

INTEREST RATES. END QUOTE.

2. THE TIMES, IN REPORTING THE INTERVENTION ANNOUNCEMENT, SIMPLY REFERS TO AN EDITORIAL ON THE PROBLEMS OF APPRECIATING STERLING. THIS ARTICLE STATES, IN PART: QUOTE: IN A SENSE THE CONCENTRATION ON THE EXCHANGE RATE FOR THE POUND AGAINST THE DOLLAR IS SOMETHING OF AN ANACHRONISM. THROUGH SO MANY STERLING CRISES THE HEADLINES HAVE RECORDED THE SLIDE IN THE DOLLAR VALUE OF THE POUND. DURING THE SECOND HALF OF LAST YEAR THE TREND FOR ONCE WAS IN THE REVERSE DIRECTION, SO THAT ONCE AGAIN THE POUND STANDS JUST SHORT OF \$2. THE ANACHRONISM DATES FROM THE PERIOD BEFORE THE PRESENT REGIME OF FLOATING EXCHANGE RATES, WHEN ALL THE MAJOR CURRENCIES HAD EXCHANGE RATES DECLARED IN TERMS OF THE DOLLAR WHICH WAS THEREFORE THE REFERENCE POINT OF THE ENTIRE SYSTEM. TODAY THAT IS NO LONGER THE CASE. THE DOLLAR'S DECLINE EXAGGERATES THE REAL REVALUATION OF STERLING AGAINST OTHER CURRENCIES THAT HAS TAKEN PLACE IN THE PAST YEAR. ...

IN DUE COURSE, HOWEVER, THE UPWARD VALUATION OF THE POUND MUST BEGIN TO UNDERMINE THE OVERSEAS PERFORMANCE OF BRITISH INDUSTRY, UNLESS THERE IS SOME SEA CHANGE IN THE CLIMATE OF BRITISH INFLATION AND PRODUCTIVITY IN RELATION TO OUR PRINCIPAL INDUSTRIAL COMPETITORS. SINCE THE BEGINNING OF THE PRESENT RECESSION IN 1973, FOR EXAMPLE, UNIT LABOUR COSTS IN THIS COUNTRY HAVE RISEN BY SOME 10 PER-
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CENT IN DOLLAR TERMS, COMPARED WITH THOSE FOR THE UNITED STATES. SINCE RELATIVE PRODUCTIVITY HAS ALSO FALLEN, IT

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IS CLEAR THAT THE PRESENT TREND OF THE EXCHANGE RATE
DOES NOT REFLECT THE UNDERLYING ECONOMIC AND INDUSTRIAL
REALITY. END QUOTE.

3. HAMISH MCRAE IN THE GUARDIAN WRITES: QUOTE: THE
ABOUT-TURN BY THE US AUTHORITIES HAS HAPPENED. YESTER-
DAY'S ANNOUNCEMENT TO SUPPORT THE DOLLAR, BACKED BY HARD
MONEY OFFERED ON THE NEW YORK FOREIGN EXCHANGE MARKET
AFTER LONDON HAD CLOSED, NOT ONLY FLIPPED ROUND THE
RATES ON THE FOREIGN EXCHANGES. IT ALSO DEMONSTRATED
THAT SOMETHING, SOMEWHERE HAS MADE THE AMERICANS MOVE.
THE NEW POLICY IS A COMPLETE REVERSAL OF ALL PRONOUNCE-
MENTS BY THE US AUTHORITIES OVER THE LAST 12 MONTHS. ...

THE AIM WAS CLEARLY TO FRIGHTEN EVERYONE AND IT CER-
TAINLY DID THAT, FOR THOUGH MANY NEW YORK BANKS HAD BEEN
ANXIOUS THAT PRESIDENT CARTER'S RETURN TO THE COUNTRY
MIGHT SIGNAL SOME CHANGE IN EXCHANGE RATE POLICY, NO-ONE
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EXPECTED ACTION WHILE HE WAS STILL OUT OF THE COUNTRY.

THE MOST COHERENT EXPLANATION FOR THE ABOUT-TURN IS
THAT ON TUESDAY PRESIDENT CARTER MET SAUDI ARABIAN LEAD-
ERS AND RECEIVED A VERY COLD WARNING ABOUT THE US ADMIN-
ISTRATION'S NEGLECT OF THE DOLLAR. SAUDI ARABIAN MONEY
FLOATING INTO THE UNITED STATES IS THE ONLY THING CUR-
RENTLY HOLDING UP THE DOLLAR. ...

THE MEASURES ANNOUNCED YESTERDAY WILL CERTAINLY WORK
FOR A WHILE. AS ARGUED IN THIS COLUMN ON DECEMBER 15,
TECHNICALLY THE TIME IS RIPE FOR THAT CLASSIC MANOEUVRE
OF THE CENTRAL BANKS, THE "BEAR TRAP." WELL, HERE IT IS.
BUT THE REAL QUESTION IS WHETHER THERE WILL BE ENOUGH
GOOD NEWS ON THE U.S. ENERGY FRONT DURING THE NEXT FEW
WEEKS TO SUSTAIN THE ADVANCE. THE LESSON OF FOREIGN EX-
CHANGE MARKET INTERVENTION HAS ALWAYS BEEN THAT IT ONLY
WORKS IF IT REINFORCES AN UNDERLYING VIEW OF THE MARKET
ITSELF. ...

THE DRAMATIC MOVEMENTS OF NEW YORK YESTERDAY, THOUGH,
ARE LIKELY TO BE REPEATED IN THE VERY MUCH WIDER EURO-
PEAN FOREIGN EXCHANGES. A FEW DAYS OF PROPER TRADING
ARE NEEDED BEFORE A CLEAR PATTERN EMERGES. END QUOTE

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